

OPINION NOT FOR PUBLICATION IN WEST'S BANKRUPTCY REPORTER:

Case: In re Kim M. Ross-Tucker, Case No. 03-01436

Opinion: Opinion Addressing Trustee's Request to Hold Debtor in Contempt and to Surcharge Debtor's Exempt Property

Decided: November 28, 2005.

Judge: S. Martin Teel, Jr.

Attorneys:

Darrell W. Clark for Bryan S. Ross, Chapter 7 Trustee

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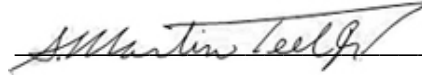
Holdings:

1. Trustee is permitted to surcharge the debtor's exempt home for an earlier \$25,000 judgment awarded to the trustee to make the estate whole and which represented amounts that the debtor dissipated from the proceeds of a lawsuit that was settled without court authorization.

2. Trustee may not recover attorney's fees as the debtor is not in civil contempt: she did not fail to comply with an order of the court, and only failed to pay a monetary judgment. Contempt sanctions ordinarily may not be used with respect to failure to pay a monetary judgment.

The opinion below is hereby signed. Dated: November 28, 2005.




S. Martin Teel, Jr.
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF COLUMBIA

In re)	
)	
KIM M. ROSS-TUCKER,)	Case No. 03-1436
)	(Chapter 7)
Debtor.)	

OPINION ADDRESSING TRUSTEE'S REQUEST TO
HOLD DEBTOR IN CONTEMPT AND TO SURCHARGE DEBTOR'S EXEMPT PROPERTY

This opinion addresses the Chapter 7 trustee's request to hold the debtor, Kim M. Ross-Tucker, in contempt and to surcharge the debtor's exempt property (her home) based on the debtor's failure to comply with a judgment awarding the trustee, pursuant to an earlier turnover motion, an amount representing proceeds of a lawsuit that the debtor failed to disclose to the trustee. The court will deny the trustee's request for contempt sanctions, but will grant the request for surcharge.

I

On October 20, 2004, Bryan S. Ross, the Chapter 7 trustee, filed a Motion for Order Directing Debtor to Turn Over and Account for Property of the Estate (DE No. 62). In that motion, the trustee alleged that the debtor failed to disclose her post-

petition receipt of \$25,000 in proceeds relating to the settlement of a lawsuit filed by the debtor against Lloyd Credle in the Superior Court for the District of Columbia, and that the debtor likewise failed to turn those funds over to the Chapter 7 trustee.

At a December 16, 2004 hearing, the court heard evidence that, when asked about the status of the lawsuit with Credle at the meeting of creditors, the debtor knowingly failed to disclose to the Chapter 7 trustee that, prior to the conversion of her case from a case under Chapter 7 to a case under Chapter 13, she had received \$25,000 in settlement funds in connection with that lawsuit. The court also heard testimony that most if not all of the settlement proceeds had been expended by the debtor prior to the conversion of her case and, although the debtor failed to disclose the existence of the funds to the Chapter 7 trustee, at least some of the settlement proceeds were used to repair the debtor's real property at 1002 Park Road, N.W., Washington, D.C., which the debtor has claimed as exempt in this bankruptcy case, and that some of the proceeds were used to pay creditors who might have otherwise been creditors in the debtor's Chapter 7 case.

In an oral opinion, the court held that, notwithstanding the use to which the debtor may have put some of the settlement proceeds, the debtor's failure to give proper notice to creditors

of the settlement with Credle, and her failure to seek court approval of its terms, rendered the debtor's \$25,000 settlement of her lawsuit with Credle an unauthorized compromise. The court further held that the funds constituted property of the estate and that the Chapter 7 trustee was accordingly entitled to a judgment against the debtor for the recovery of the \$25,000.

The opinion was followed by a final judgment (DE No. 79, entered December 23, 2004), from which no appeal was ever taken. Accordingly, the court's determination that the debtor was unauthorized to enter into the settlement with Credle and that the Chapter 7 trustee is entitled to a recovery of the \$25,000 representing estate property dissipated by the debtor is law of the case.

On February 23, 2005, the trustee filed a Motion to Show Cause Why Debtor Should Not be Held in Contempt for Failing to Pay Funds Ordered by the Court to be Turned Over to the Trustee (DE No. 84). In addition to seeking an order directing the debtor to show cause why she should not be held in contempt for failure to pay the funds as directed by the Court's December 23, 2004 judgment, the motion further requested that, as a sanction for the debtor's failure to pay the funds to make the estate whole, the court consider surcharging the debtor's exempt property. Specifically, the trustee requested that the court surcharge the debtor's exemption of her home, real property

located at 1002 Park Road, N.W., Washington, D.C., so that the trustee may record the judgment as a lien against the real property and thereafter sell the property through the foreclosure process. Having held a hearing to address the Chapter 7 trustee's request to surcharge the debtor's exempt property on June 7, 2005, the court took the trustee's motion under advisement.

In the meantime, and based, inter alia, upon the same conduct complained of by the Chapter 7 trustee in seeking a turnover of the \$25,000 from the debtor, the U.S. Trustee commenced an adversary proceeding seeking an order denying the debtor a discharge in bankruptcy (DE No. 81, filed January 21, 2005, commencing Adv. Pro. No. 05-10004). At a September 19, 2005 hearing, the court issued an oral opinion granting summary judgment in the U.S. Trustee's favor, followed by a judgment denying the debtor a discharge in bankruptcy. In its September 19, 2005 oral opinion, the court held, inter alia, that the debtor violated 11 U.S.C. § 727(a)(4) by knowingly and fraudulently, in or in connection with her bankruptcy case, making a false oath by testifying falsely about the status of her lawsuit against Credle at the meeting of creditors, thereby concealing property of the estate from the Chapter 7 trustee. No appeal was taken from the court's determination that the debtor violated 11 U.S.C. § 727(a)(4) by testifying falsely at the

meeting of creditors warranting a denial of discharge to the debtor in bankruptcy, and the court's opinion remains law of the case.

II

The debtor objects to the trustee's motion to surcharge her exempt property because (1) there has been no finding that the debtor engaged in willful misconduct or fraudulent behavior, and (2) allowing the Chapter 7 trustee to surcharge a debtor's exempt assets while the office of the U.S. Trustee pursues a denial of discharge is repugnant and inconsistent in this case (DE No. 95, filed May 25, 2005). For reasons explained in more detail below, the court rejects the debtor's arguments and will, in the exercise of its discretion, permit the trustee to surcharge the debtor's exempt property in the amount of the \$25,000 judgment, but the court will not hold the debtor in contempt.

A.

A "bankruptcy court may equitably surcharge a debtor's statutory exemptions when reasonably necessary both to protect the integrity of the bankruptcy process and to ensure that a debtor exempts an amount no greater than what is permitted by the exemption scheme of the Bankruptcy Code." Latman v. Burdette, 366 F.3d 774, 786 (9th Cir. 2004); In re Karl, 313 B.R. 827, 831 (Bankr. W.D. Mo. 2004) ("When a debtor's contemptuous conduct involves the suppression of estate property, or when a debtor

fails to adequately explain its loss, a court may surcharge the debtor's exemptions in an effort to prevent a fraud on the bankruptcy court and to protect creditors by preventing the debtor from sheltering more assets than permitted by the Bankruptcy Code.").¹

Although the trustee's motion characterizes its request for a surcharge as a sanction, "the purpose is not to 'punish' the debtor, but to reach an equitable result by preserving the spirit of the Bankruptcy Code and the creditors' reasonable expectations in the event of liquidation." Id. (surcharging debtors' homestead exemption to the extent of the value of a vehicle based on the debtors' failure to turn the vehicle over to the trustee and for thwarting the trustee's efforts at recovering the vehicle); Latman, 366 F.3d at 783 ("The aim of this remedy was not to punish the [debtors], but instead was to protect the creditors of the bankruptcy estate. The surcharge remedy maximized the value of the bankruptcy estate, by ensuring that the [debtors] did not exclude from their estate assets valued in excess of their permitted exemptions.").

If the debtor is permitted to retain the benefit of the \$25,000 in settlement proceeds -- estate property that she failed

¹ Although Karl involved a failure to comply with a court order, giving rise to a finding of civil contempt, the rationale of Karl and the other decisions authorizing surcharge of the debtor's exemptions does not require the existence of contempt as a condition to granting surcharge.

to turn over to the trustee and which should have been available for distribution to creditors in this bankruptcy case -- and at the same time is permitted to safeguard the full value of her claimed homestead exemption, she [has] "pocket[ed] funds that belonged to creditors by sheltering more assets than permitted by the exemption scheme of the Bankruptcy Code." Id. at 783. Allowing the trustee to surcharge the debtor's exempt property in this bankruptcy case will "simply ensure[] that [the debtor] retain[s] the full value, but no more than the full value, of [her] permitted exemptions." Id. at 785. This is an equitable result under the circumstances.

The debtor argues that her exempt assets should not be surcharged because there has been no finding that the debtor engaged in willful misconduct or fraudulent behavior. She urges that her failure to seek approval of the settlement with Credle arose from her ignorance of her obligation first to seek such approval from the court; that she had scheduled the lawsuit on her schedules; and that the proceeds were used in large part to pay creditors who would have otherwise had claims to be paid in the Chapter 7 case. The court, however, has previously found, and it is law of the case, that the debtor's failure to disclose the existence of the settlement proceeds to the Chapter 7 trustee at the meeting of creditors constituted a violation of § 727(a)(4)(A) warranting the denial of a discharge to the debtor

in this bankruptcy case. Implicit, if not explicit, in the denial of a discharge, is a finding that the debtor has in some way abused the bankruptcy process. Latman, 366 F.3d at 782 (denial of discharge is a punitive remedy designed to "punish[] debtors for misconduct in the bankruptcy process."). The trustee's claim to the \$25,000 in this case "arises from the debtor['s] willful breach of a positive statutory duty to deliver and account for property of the estate," and as such involves at least some measure of wrongful conduct on the debtor's part. In re Ward, 210 B.R. 531, 538 (Bankr. E.D. Va. 1997).

Even if the court had made no express finding that the debtor engaged in "willful misconduct or fraudulent behavior," it is law of the case that the \$25,000 in settlement proceeds retained by the debtor was property of the estate that should have been disclosed to the Chapter 7 trustee and that the debtor was required to pay an amount equal to that \$25,000 to the Chapter 7 trustee to make the estate whole. Although the debtor's conduct may be comparatively less offensive than that of debtors who engage in more calculated schemes to defraud creditors through the concealment of assets, the degree of wrongdoing attributable to the debtor's conduct is not the only relevant factor the court must consider. It is equally important to assess the extent to which unsecured creditors have been unfairly prejudiced by the debtor's willful conduct, and whether,

under the circumstances, it is fair to permit the debtor to retain the benefit of funds that the bankruptcy court has determined belonged to the estate. Given that the court has, in fact, found that the debtor engaged in willful misconduct, and given that there are other relevant factors that support the remedy of surcharge in this case (such as unfair prejudice to creditors arising from dissipation of \$25,000 that would have been available to creditors), the court rejects the debtor's argument that the remedy of surcharge is inappropriate because there has been no finding of willful misconduct or fraudulent behavior.

The court rejects the argument that surcharge is inappropriate because the estate was not harmed to the extent that claims were paid that would have been entitled to payment in the Chapter 7 case. That argument was raised by the debtor and rejected by the court when the Chapter 7 trustee pursued his Motion for Order Directing Debtor to Turn Over and Account for Property of the Estate. The judgment for \$25,000 precludes the debtor from raising the issue anew. Moreover, those creditors whose claims remain unpaid were deprived by the debtor's dissipation of the \$25,000 of a dividend through distribution of that \$25,000. The proceeds in large part went to claims for repairing and improving the debtor's home (the exempt property at issue), and to mortgage charges against it, and that is a factor

that weighs in favor of the court's determination that the exempt property ought to be made subject to surcharge. In any event, because the debtor was found to be at fault in this case, both by way of the judgment against her for \$25,000 and by way of the denial of discharge, matters that remain law of the case, the trustee ought not be put to the expensive burden of an inquiry regarding what claims were fully paid by the debtor out of the \$25,000,² whether they would have been unsecured claims had they not been paid such that they would have shared in a Chapter 7 distribution,³ and what *pro rata* distributions would have been

² If an unsecured claim was only partially paid by the debtor, the holder of the claim would still be entitled to a *pro rata* distribution in the Chapter 7 case up to the unpaid amount of its claim. Moreover, because holders of claims fully paid would have no occasion to file a proof of claim in the Chapter 7 case, it is entirely speculative whether the holders of such claims that were incurred after the commencement of the case would have filed claims in the Chapter 7 case had their claims not been paid.

³ Fully secured claims would be unaffected by the Chapter 7 case, and would not receive a distribution of the \$25,000 by the Chapter 7 trustee. One entity paid after receipt of the \$25,000 was the debtor's mortgagee, Bank of America. Moreover, some of the claims paid were for repair work on the debtor's home for which a mechanic's lien could have been obtained. The debtor fully exempted her home, and it ceased to be property of the estate when no one timely objected to the claimed exemption. 11 U.S.C. § 522 paragraphs (b) and (1). As no longer property of the estate, the home became unprotected by the stay of 11 U.S.C. § 362(a) barring certain acts against property of the estate. See 11 U.S.C. § 362(c)(1). Accordingly, the entities performing repair work after the debtor received the \$25,000 could have obtained mechanics' liens without violating the automatic stay. And those who performed work before the debtor received the \$25,000 may or may not have had mechanics liens: the record is silent on that issue.

made on such claims had they not been paid. In any event, the debtor has not adduced satisfactory evidence to provide answers to those issues.

The debtor further argues that allowing the Chapter 7 trustee to surcharge the debtor's exempt assets while the office of the U.S. Trustee pursues a denial of a discharge to the debtor is repugnant and inconsistent with this case. In support of this argument, the debtor seeks to distinguish the facts of this case from those of Latman, principally based on the notion that the debtors' concealment of assets in Latman involved more egregious conduct than was found in the instant case, and that the nature of the property sought to be surcharged in that case renders the cases distinguishable. First, although the U.S. Trustee's denial of discharge complaint had yet to be resolved at the time the debtor filed her brief in this matter, the U.S. Trustee has since prevailed in his effort, a fact that weighs against the debtor in resolving the instant dispute. Furthermore, although distinguishable on its facts in some respects, this case and Latman share one critical fact in common: both cases involve creditors who were wrongfully deprived of a possible distribution of funds due to the debtor's knowing concealment of an estate asset from the Chapter 7 trustee.

Given that the debtor has thus far failed to satisfy the court's order granting recovery of \$25,000 pursuant to the

Chapter 7 trustee's turnover motion, the most equitable solution is to allow the trustee to surcharge the debtor's exempt property in an amount equal to that owing to the Chapter 7 trustee.

B.

The question remains whether the debtor should be held in civil contempt for failing to comply with the turnover order. The turnover order was not directed to a specific *res* still in the debtor's possession as the proceeds of the settlement of the lawsuit had been dissipated. The judgment granting the turnover motion was thus cast in the nature of a monetary judgment to make the estate whole. A contempt motion is not an appropriate vehicle for enforcing a monetary judgment. See Patterson v. America's Voice, Inc. (In re America's Voice, Inc.), 2000 WL 33529764 (Bankr. D.D.C. 2000). Although the court in Karl, 313 B.R. at 832, awarded attorney's fees to a trustee in addition to granting a surcharge of exempt property, the debtors there had failed to comply with orders to turn over a specific *res*, a pickup truck, and thus were held in civil contempt. An award of attorney's fees is appropriate as a compensatory sanction for damages (the incurring of attorney's fees) arising from civil contempt. Here, the debtor did not fail to comply with an order of the court and instead simply failed to pay a monetary judgment. She is thus not in civil contempt, and the trustee points to no statute or common law exception varying the ordinary

American rule that parties bear their own attorney's fees.

III

An order follows.

[Signed and dated above.]

Copies to:

All Counsel of Record; Chapter 7 Trustee; Debtor; U.S. Trustee.